

**STATE OF WASHINGTON
OFFICE OF THE INSURANCE
COMMISSIONER**



**FINANCIAL EXAMINATION
OF
Catholic Foundation of the Spokane Diocese
Spokane, Washington**

AS OF DECEMBER 31, 2002

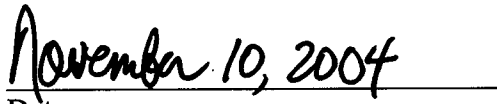
Catholic Foundation of the Spokane Archdiocese
Order No. G04-77
Exhibit A

CHIEF EXAMINER'S AFFIDAVIT

I hereby certify that the attached Report of Examination shows the financial condition and affairs of the CATHOLIC FOUNDATION OF THE SPOKANE DIOCESE of Spokane, Washington as of December 31, 2002.

A handwritten signature in black ink, reading "Patrick H. McNaughton", written over a horizontal line.

Patrick H. McNaughton
Chief Examiner

A handwritten date in black ink, reading "November 10, 2004", written over a horizontal line.

Date

CATHOLIC FOUNDATION OF THE SPOKANCE DIOCESE

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SALUTATION

Seattle, Washington
October 28, 2004

The Honorable Mike Kreidler, Commissioner
Washington State Office of the Insurance Commissioner (OIC)
Insurance 5000 Building
5000 Capitol Blvd.
Tumwater, WA 98501

Dear Commissioner Kreidler:

In accordance with your instructions and in compliance with the statutory requirements of Chapter 48.38 RCW, Charitable Gift Annuity Business, an examination was made of the corporate affairs and financial records of

Catholic Foundation of the Spokane Diocese
of
Spokane, Washington

hereinafter referred to as "Catholic Foundation" or the "Foundation" at its home office, located at 1023 West Riverside Avenue, Spokane, Washington 99210.

This report of examination is respectfully submitted showing the condition of Catholic Foundation as of December 31, 2002.

SCOPE OF EXAMINATION

This examination covers the period January 1, 1998 through December 31, 2002. The examination was conducted in accordance with statutory requirements contained in the Revised Code of Washington (RCW) and the guidelines recommended by the National Association of Insurance Commissioners (NAIC) Financial Condition Examiners Handbook. We focused our review and testing on the Catholic Foundation's management, operations, and reporting of the charitable gift annuity business as considered necessary to ascertain the financial condition of the organization and conformity with the related laws. These matters are discussed in this report. The examination was conducted at the Spokane office of the Catholic Foundation by examiners from the state of Washington.

INSTRUCTIONS

The examiners reviewed the organization's filed 2002 Annual Report as part of the statutory examination. This review was performed to determine if the organization completed the Annual Report in accordance with the Annual Report Instructions published by the OIC and to verify that the organization's accounts and records were prepared and maintained in accordance with Title 48 of the RCW.

The following summarizes the exceptions noted while performing this review.

1. Annuities Payable/Reserves

The Foundation did not report the reserve amount calculated by its actuary plus a surplus of ten percent of the calculated reserve, or a total amount of \$313,981, as an annuities liability. This resulted in an understatement of the reported liabilities by \$313,981 as of December 31, 2002. Consequently, the understated liability resulted in overstating temporarily restricted net assets by \$313,981. The Foundation, therefore, did not comply with the accounting and reporting principles or practices prescribed or permitted by the OIC.

RCW 48.38.020 states that:

- (1) "Upon granting to such insurer or institution under RCW 48.38.010 a certificate of exemption to conduct a charitable gift annuity business, the insurance commissioner shall require it to establish and maintain a separate reserve fund adequate to meet the future payments under its charitable gift annuity contracts."
- (3) "The amount of the separate reserve fund shall be:
 - (a) For contracts issued prior to July 1, 1998, not less than an amount computed in accordance with the standard of valuation based on the 1971 individual annuity mortality table with six percent interest for single premium immediate annuity contracts and four percent interest for all other individual annuity contracts;

- (b) For contracts issued on or after July 1, 1998, in an amount not less than the aggregate reserve calculated according to the standards set forth in RCW 48.74.030 for other annuities with no cash settlement options;
- (c) Plus a surplus of ten percent of the combined amounts under (a) and (b) of this subsection.”

In addition, RCW 48.38.010 states, “The commissioner may grant a certificate of exemption to any insurer or educational, religious, charitable, or scientific institution conducting a charitable gift annuity business: (10) Which: (a) Files with the insurance commissioner on or before March 1 of each year a copy of its annual statement prepared pursuant to the laws of its state of domicile, as well as such other financial material as may be requested...”

The Foundation is instructed to report the statutory reserve amount on its financial statements in compliance with RCW 48.38.010(10)(a) and RCW 48.38.020(1) and (3).

2. Assets of the Separate Reserve Fund

The annuity funds were invested and commingled with other funds in the Spokane Catholic Investment Trust. The Foundation was not in compliance with the requirements stipulated in RCW 48.38.020(1) and (2)(a) because the assets of the annuity reserve fund were not physically segregated from the other assets of the organization.

RCW 48.38.020(1) states that, “Upon granting to such insurer or institution under RCW 48.38.010 a certificate of exemption to conduct a charitable gift annuity business, the insurance commissioner shall require it to establish and maintain a separate reserve fund adequate to meet the future payments under its charitable gift annuity contracts.”

RCW 48.38.020(2)(a) states that, “The assets of the separate reserve fund: (a) Shall be held legally and physically segregated from the other assets of the certificate of exemption holder.”

The Foundation is instructed to develop a system for accounting, investing, and reporting of its charitable gift annuity business to ensure its compliance with RCW 48.38.010(10)(a) and RCW 48.38.020(2)(a).

3. Net Assets: Unrestricted, Temporarily Restricted and Permanently Restricted

The total of net assets shown in the December 31, 2002 Annual Report, amounting to \$13,569,833, was inaccurate. Reported amounts for unrestricted, temporarily restricted and permanently restricted net assets did not agree with the Foundation’s records. There were instances wherein amounts in the supporting schedules did not agree with the balance sheet detail, and certain fund balances were not reported at all or misclassified in the supporting schedules. The Foundation did not comply with the accounting and reporting principles or practices prescribed or permitted by the OIC.

As a result of the examination, total net assets reported in the Annual Report were increased to \$13,697,176 to agree with the Foundation's accounting records as of December 31, 2002. Also, the unrestricted net assets were increased from \$443,356 to \$780,291. The Foundation, after the examination adjustments to the 2002 Annual Report, was in compliance with RCW 48.38.010 (6); its unrestricted net assets as of December 31, 2002 were in excess of the required minimum amount of \$500,000.

RCW 48.38.010 states that, "The commissioner may grant a certificate of exemption to any insurer or educational, religious, charitable, or scientific institution conducting a charitable gift annuity business: (10) Which: (a) Files with the insurance commissioner on or before March 1 of each year a copy of its annual statement prepared pursuant to the laws of its state of domicile, as well as such other financial material as may be requested . . ."

The Foundation is instructed, pursuant to Chapter 48.38 RCW, to develop a system for accounting and reporting of its charitable gift annuity business to ensure its compliance with the principles or practices prescribed or permitted by the Washington State Office of the Insurance Commissioner. The system should include procedures for appropriate review, by staff other than the report preparer, to assure the completeness and accuracy of the Annual Report.

HISTORY

The Foundation is a separate nonprofit corporation, governed by a Board of Trustees. The Foundation was organized under the laws of the state of Washington on January 28, 1981. The Foundation's mission is to provide financial assistance to Catholic programs, parishes, schools and services within Eastern Washington. Its functions include: (1) the administration of property donated to the Foundation, and (2) the distribution of property to qualified religious, educational and other charitable organizations with the terms of gifts, bequests or devices to the Foundation, or in accordance with the determinations of the Board of Trustees.

MANAGEMENT

The management and administration of the affairs of the Foundation are the responsibility of the Board of Trustees. The Board of Trustees consists of twenty-one (21) volunteer members. The Trustees lend their time and talents to the committees necessary to perform the work of the Foundation. Current Trustees include:

Rich Algeo
Joanne Cipolla
Virgil Emery
Bob Laabs
Jane Parry

Dave Barber
Dr. Tom Driscoll
Art Griff
Scott McGann
Paul Pimentel

Gary Brajcich
Garrick Dung
Bob Hailey
John Moloney, Jr.
Peggy Rolando

Paul Russell
Nancy Voorhees

Barbara Savage
Martin Weber

Rich Umbdenstock
Dominic Zamora

AFFILIATED COMPANIES

The Foundation is a separate corporation under the laws of the state of Washington and is affiliated with the Catholic Diocese of Spokane. Pursuant to the Foundation's Bylaws, the Bishop of Spokane, or his equivalent in office, has ultimate authority and responsibility over the Catholic Foundation. The Bishop of Spokane has sole responsibility over the affairs of the Foundation and has the authority to delegate said authority to the Board of Trustees to create effective and efficient management of the Foundation.

CORPORATE RECORDS

Minutes: The Board of Trustees meets at least quarterly during the year to discuss that business which is pertinent to the Foundation. Minutes of the quarterly meetings were prepared, approved and retained. No exceptions were noted.

Conflicts of Interest: The Foundation's conflict of interest policy notes, "(1) all employees must avoid activities or relationships that conflict with Catholic Charities' interests or adversely affect Catholic Charities' reputation, and (2) employees must disclose actual or potential conflicts to their supervisor as soon as they become aware of them." No exceptions were noted.

Internal Policies and Controls: An Investment Policy is established and approved by the Board of Trustees and the Investment Committee. The purpose of the policy statement is to outline the goals, objectives, and specific investment guidelines of the Spokane Catholic Investment Trusts. The policy establishes clear authority parameters and restrictions for the Board of Trustees, Investment Committee and Investment Managers. No exceptions were noted.

TERRITORY AND PLAN OF OPERATION

The Catholic Foundation was established in 1981. It was formed to provide financial assistance to Catholic programs and services in the Diocese of Spokane. The Foundation's assets are held in many separate endowment accounts which provide income for parishes, schools, agencies and diocesan programs. The Foundation was granted a Certificate of Exemption Number 35 to conduct a Charitable Gift Annuity business in the state of Washington by OIC on November 5, 1991. There were fifteen (15) in-force annuity contracts as of December 31, 2002. All of the 15 annuity contracts were issued to residents of the state of Washington, and included: thirteen (13) One Life (single) Annuities, Immediate Payments; one (1) Two Lives (joint) Annuity, Immediate Payments; and one (1) Two Lives (joint) Annuity, Deferred Payments.

INTERNAL SECURITY

External Audit Function: The firm of Moss-Adams LLP audited the financial statements of the Catholic Foundation of the Spokane Diocese and issued unqualified opinions for the fiscal years June 30, 2002 and 2001.

Internal Audit Function: The Foundation has no internal audit department.

Asset Custodial Function: All funds of the Catholic Foundation are held and commingled in the Spokane Catholic Investment Trust (the Trust) in violation of RCW 48.38.020(2)(a). The Trust was established for the purpose of investing funds for charitable organizations within the Catholic Diocese of Spokane. Members of the Trust include the Catholic Diocese of Spokane, the Catholic Foundation, Catholic Charities, Inc., Catholic Cemeteries of Spokane, Morning Star Boys Ranch, Immaculate Heart Retreat Center Foundation, and Gonzaga Preparatory School (a non-related entity). The Investment Trust records and financial statements for December 31, 2002 and 2001 were audited by Moss-Adams. An unqualified opinion report was issued to the Board of Directors on March 28, 2003. (See "INSTRUCTION" No.2)

GROWTH OF COMPANY

The growth of the Foundation for the past five years is reflected in the following exhibits. All information was compiled from the Foundation's filed financial statements as of fiscal years ending June 30. (Please note that this information is provided based on the company's fiscal year-end which is different than the examination as-of date.)

Schedule 1

Fiscal Year	Assets	Liabilities	Total Net Assets	Total Net Assets Allocated Into:		
				Unrestricted	Temporarily Restricted	Permanently Restricted
2002	\$14,845,487	\$21,696	\$14,823,791	\$649,400	\$6,872,229	\$7,302,162
2001	15,175,217	2,316	15,172,901	663,988	6,881,894	7,627,019
2000	12,438,881	12,381	12,426,500	626,691	4,310,453	7,489,356
1999	12,730,866	115,281	12,615,585	599,501	4,209,375	7,806,709
1998	12,176,418	557,203	11,619,215	519,954	3,854,426	7,244,835

Schedule 2

	<u>FY 2002</u>	<u>FY 2001</u>	<u>FY 2000</u>	<u>FY 1999</u>	<u>FY 1998</u>
Changes in unrestricted NA					
Revenues and gains (loss)	(\$25,245)	\$33,023	\$38,689	\$149,186	\$1,828,989
NA released from restrictions	871,158	871,348	924,657	849,123	
Expenses	(860,501)	(867,074)	(936,156)	(918,762)	(798,142)
Increase (decrease) in unrestricted NA	(\$14,588)	\$37,297	\$27,190	\$79,547	\$1,030,847
Changes in temporarily restricted NA	(9,665)	2,571,441	6,199	354,949	
Changes in permanently restricted NA	(324,857)	137,663	(222,474)	561,874	
Increase (decrease) in net assets	(\$349,110)	\$2,746,401	(\$189,085)	\$996,370	\$1,030,847
Net assets at beginning of period	15,172,901	12,426,500	12,615,585	11,619,215	10,588,368
Net assets at end of year	<u>\$14,823,791</u>	<u>\$15,172,901</u>	<u>\$12,426,500</u>	<u>\$12,615,585</u>	<u>\$11,619,215</u>
Number of gift annuity contracts at end of year	15	12	7	9	12

SUBSEQUENT EVENTS

An Order Suspending Certificate of Exemption Number 35 was signed and entered on April 4, 2003 by the OIC. The basis for the order is that the Foundation failed to maintain minimum unrestricted net assets of \$500,000 which is a violation of RCW 48.38.010(6). (See "INSTRUCTIONS" No. 3)

FINANCIAL STATEMENTS
As of DECEMBER 31, 2002

The following statements reflect the financial condition of the Foundation as determined by this examination.

Balance Sheet

	<u>Balance Per</u> <u>Annual</u> <u>Report</u>	<u>Adj.</u> <u>Notes</u>	<u>Examination</u> <u>Adjustments</u>	<u>Adjusted</u> <u>Balance</u>
<u>ASSETS</u>				
Cash and cash equivalents	\$163,969			\$163,969
Investments	12,389,712	Note 3	\$441,324	12,831,036
Prepaid expenses	14,762			14,762
Accounts receivable	26,557			26,557
Fund transfer	974,833			974,833
Total Assets	<u>\$13,569,833</u>		<u>\$441,324</u>	<u>\$14,011,157</u>
<u>LIABILITIES</u>				
Accounts payable	0			
Annuities payable	0	Note 1	313,981	313,981
Total Liabilities	<u>0</u>		<u>313,981</u>	<u>313,981</u>
<u>NET ASSETS</u>				
Unrestricted	443,356	Note 2	336,935	780,291
Temporarily restricted	6,236,167	Note 2	(93,652)	6,142,515
Permanently restricted	6,890,310	Note 2	(115,940)	6,774,370
Total Net Assets	<u>13,569,833</u>		<u>127,343</u>	<u>13,697,176</u>
Total Liabilities and Net Assets	<u>\$13,569,833</u>		<u>\$441,324</u>	<u>\$14,011,157</u>

Adjustment Notes:

Note 1 – To recognize the statutory annuity reserves as a liability. (See “INSTRUCTIONS” No.1)

Note 2 – To recognize examination adjustments to the Annual Report to agree with the Foundation’s accounting records. The increases or decreases to net assets consisted of balances not reported, balances erroneously accounted for, and annuity reserves reported as net assets in the Annual Report. (See “INSTRUCTIONS” No. 3)

Note 3 – To recognize the aggregate results of the examination adjustments, Note 1 and Note 2, to total assets. This adjustment represented the total investments not reported in the Annual Report by the Foundation. (See “INSTRUCTIONS” No. 3)

Statement of Financial Activity and Changes in Net Assets

	<u>Balance Per Company</u>	<u>Adj. Notes</u>	<u>Examination Adjustments</u>	<u>Adjusted Balance</u>
Total revenues	\$84,195			\$84,195
Total expenses	(36,213)			(36,213)
Increase (decrease) in net assets	\$47,982		\$0	\$47,982
Net assets at beginning of year	13,521,851			13,521,851
Changes in net assets per examination			127,343	127,343
Net assets at end of year	<u>\$13,569,833</u>	Note 4	<u>\$127,343</u>	<u>\$13,697,176</u>

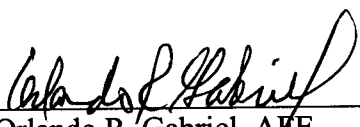
Adjustment Notes:

Note 4 – To recognize changes in net assets per examination (See Note2 on page 7).

ACKNOWLEDGEMENT

The cooperation and assistance of the officers and employees of the Foundation during the examination are hereby acknowledged.

In addition to the undersigned, Michael V. Jordan, CPA, CFE, MHP, Assistant Chief Examiner, from the Washington State Office of the Insurance Commissioner, participated in the examination and the preparation of this report.



Orlando R. Gabriel, AFE
Examiner-in-Charge
State of Washington

AFFIDAVIT OF EXAMINER IN CHARGE

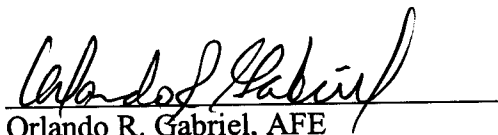
STATE OF WASHINGTON)

) ss

COUNTY OF KING)

Orlando R. Gabriel, AFE, being duly sworn, deposes and says that the foregoing report subscribed by him is true to the best of his knowledge and belief.

He attests that the examination of the Catholic Foundation of the Spokane Diocese was performed in a manner consistent with the standards and procedures required or prescribed by the Washington State Office of the Insurance Commissioner (OIC) and the National Association of Insurance Commissioners (NAIC).

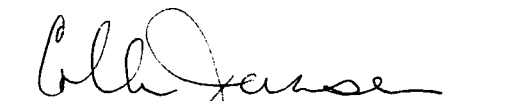


Orlando R. Gabriel, AFE

Examiner-in-Charge

State of Washington

Subscribed and sworn to before me on this 9th day of November, 2004.



Notary Public in and for the

State of Washington

Residing at Seattle.

